In the Supreme Court of the United States

OCTOBER TERM, A. D. 1944.

No. 496

THE TERMINAL AND SHAKER HEIGHTS REALTY CO.,
Petitioner,

vs.

CHARLES L. BRADLEY and
JOHN P. MURPHY,
Respondents.

PETITION FOR WRIT OF CERTIORARI
and
BRIEF IN SUPPORT OF PETITION.

ROBERT J. BULKLEY,
JAMES A. BUTLER,
Bulkley Bldg., Cleveland 15, Ohio,
ROBERT W. PURCELL,
Terminal Tower, Cleveland 13, Ohio,
Attorneys for The Terminal and Shaker Heights Realty Company.

THE GATES LEGAL PUBLISHING CO., CLEVELAND, OHIO—MAIN 5647

INDEX.

AUTHORITIES CITED.

Cases.

Statutes.

In the Supreme Court of the United States

OCTOBER TERM, A. D. 1944.

No. . . . . .

THE TERMINAL AND SHAKER HEIGHTS REALTY CO.,
Petitioner,

vs.

CHARLES L. BRADLEY and
JOHN P. MURPHY,
Respondents.

PETITION FOR WRIT OF CERTIORARI.

To the Honorable, The Chief Justice and the Associate Justices of the United States:

Petitioner, The Terminal and Shaker Heights Realty Company, hereby petitions for the issuance of a Writ of Certiorari to review the judgment of the United States Circuit Court of Appeals for the Sixth Circuit, whose judgment was made final on June 26, 1944, when it denied a rehearing of its decision of April 21, 1944, affirming the judgment below.

STATEMENT OF THE MATTER INVOLVED.

This is a controversy arising out of the corporate reorganization proceedings of The Higbee Company pursuant to Chapter X of the Bankruptcy Act which has been pending in the United States District Court for the Northern District of Ohio, Eastern Division.

Respondents Bradley and Murphy filed their proofs of claim, each claiming to be the owner of a one-half undivided interest in certain Higbee securities, having acquired such interests from George and Frances Ball

Foundation by bill of sale dated June 4, 1937. It is not disputed that Bradley and Murphy have the naked legal title to the securities (R. 2). The securities represent control of the Higbee Company and have a current market value of around $1,500,000.

Petitioner The Terminal and Shaker Heights Realty Company (formerly known as Midamerica Corporation and hereinafter referred to as "Midamerica") filed its proof of claim (R. 51) asserting that Higbee was indebted to Midamerica as the equitable owner of the same Higbee securities. Such equitable ownership springs from the fiduciary relationship to petitioner occupied by respondents C. L. Bradley and J. P. Murphy, and the breach of the fiduciary obligations incident to such relationship at the time of and subsequent to their purchase of the securities from the George and Frances Ball Foundation.

The conflicting proofs of claim in the reorganization proceedings and the answers thereto created the issues upon which this case was tried.

The Higbee securities, the equitable ownership of which is the subject of this litigation, are the following:

$69,673.71	participation in $523,043.51 Higbee Company note due March 1, 1934
$1,292,534.74	Higbee Company subordinated note due March 1, 1934
$258,506.94	Higbee Company subordinated note due March 1, 1934
100,000	shares Higbee Company common stock.

Despite the change in the form of the securities, which has been provided by a plan of reorganization, they will be referred to herein merely as the "Higbee securities."

In the courts below Robert R. Young, Allan P. Kirby and Frank F. Kolbe also filed proofs of claim charging that Bradley and Murphy had violated fiduciary duties to them individually when they purchased the Higbee securities from Ball Foundation. The conflicting claims were tried

simultaneously and the hearing on all claims was reported in a single record. The Circuit Court of Appeals held in favor of Bradley and Murphy. Young, Kirby and Kolbe have not filed petitions for writs of certiorari. Young and Kirby, however, are the controlling stockholders of Midamerica and as such they will be frequently referred to in the brief in support of this petition.

JURISDICTION INVOKED.

The jurisdiction of this Court to grant the Writ is invoked under 240 (a) of the Judicial Code, 28 U. S. C. A., Sec. 347(a). The judgment of the U. S. Circuit Court of Appeals for the Sixth Circuit affirming the decision below was rendered April 21, 1944 (R. p. 560) and was made final by the denial of the Petition for Rehearing on June 26, 1944 (R. p. 581). This petition is filed within the statutory period.

OPINIONS BELOW.

The opinion below of the District Court was published. It appears in 50 Fed. Supp. 114 and in the Record at page 518. The opinion of the Circuit Court of Appeals is published in the Advance Sheets of the Federal Reporter 142 F. (2d) 658, and appears in the Record at page 560.

THE QUESTIONS PRESENTED.

1. Can an executive officer and director defend his acquisition of securities representing a conflicting interest against the employer corporation's claim of constructive trust on the ground that a court found, two years after he acquired the conflicting interest, that the corporation's interest in the subject of the asserted trust was not substantial?

2. Does estoppel bar the claim of a corporation to impress a constructive trust upon securities acquired by an executive officer and director because he changed his posi-

tion to his detriment by paying a large sum to certain preferred stockholders to buy their pending appeal in a bankruptcy reorganization proceeding so that he might dismiss it, and thereafter borrowed money to pay, in accordance with its terms, a note which he had given as part of the purchase price of the securities, the note having been acquired by the corporation in the meantime?

3. Does federal procedure permit a Circuit Court to bar an appellant's claim on the ground of laches when the appellant in filing its claim, relied upon and followed the orders of the District Court in a bankruptcy reorganization, and when the Master's finding against the defense of laches was confirmed by the District Judge, and appellees took no exception to such finding nor to the order confirming it?

REASONS FOR ALLOWANCE OF THE WRIT.

Important and interesting questions arising out of a major bankruptcy proceeding are here presented. These questions are based upon conceded facts. They involve broad principles governing the fiduciary responsibility of officers and directors to their corporations, with particular reference to conflicts of interest growing out of changes in corporate relations brought about in bankruptcy reorganization. They also involve an important matter of federal procedure.

In this case the Sixth Circuit Court of Appeals has found that corporate officers had put themselves in a position of conflict adverse to the interests of their corporation, but relieved the officers from accounting for the profits thus acquired largely on the ground that the corporation's interest in the matter had, two years after the conflict arose, been adjudicated to be nominal. This decision is in conflict with the ruling of the Second Circuit U. S. Court of Appeals in the case of *Irving Trust Co. vs. Deutsch*, 73 F. (2d) 121, decided in 1934. In that case officers and directors of a corporation which went into bankruptcy were held accountable by constructive trust in favor of their corporation by

reason of putting themselves in a position of conflict adverse to the interests of their corporation. The court there held that no circumstances should relieve such officers from accounting for the profits thus acquired. In so holding the court quoted the classic sentence from Judge Cardozo's opinion in *Meinhard vs. Salmon,* 249 N. Y. 258, as follows:

> "Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions."

The rule of the Second Circuit Court was followed without limitation in *In re Commercial Tobacco Co.,* 34 Fed. Supp. 304 (D. C. S. D. N. Y. 1940). Whether litigants are to be governed by the rule of "uncompromising rigidity" of the Second Circuit Court of Appeals or that of "disintegrating erosion of particular exceptions" here adopted by the Sixth Circuit should be settled by the Supreme Court.

The conduct of common officers of two corporations in bankruptcy reorganization and their right to influence the outcome of the proceedings after acquiring a conflicting interest in one of the corporations during the course of the reorganization, is a matter of great general interest. So far as we can find, the Supreme Court has not passed upon these questions.

PRAYER FOR RELIEF.

Wherefore, the petitioner, by its counsel, prays the issuance of a Writ of Certiorari to the U. S. Circuit Court of Appeals for the Sixth Circuit to the end that the judgment may be reversed and for such other relief as to the court may seem fit.

Robert J. Bulkley,
James A. Butler,
Robert W. Purcell,
Attorneys for The Terminal and Shaker Heights Realty Company.

In the Supreme Court of the United States

OCTOBER TERM, A. D. 1944.

No. .....

THE TERMINAL AND SHAKER HEIGHTS REALTY CO.,
Petitioner,

vs.

CHARLES L. BRADLEY and
JOHN P. MURPHY,
Respondents.

BRIEF IN SUPPORT OF PETITION.

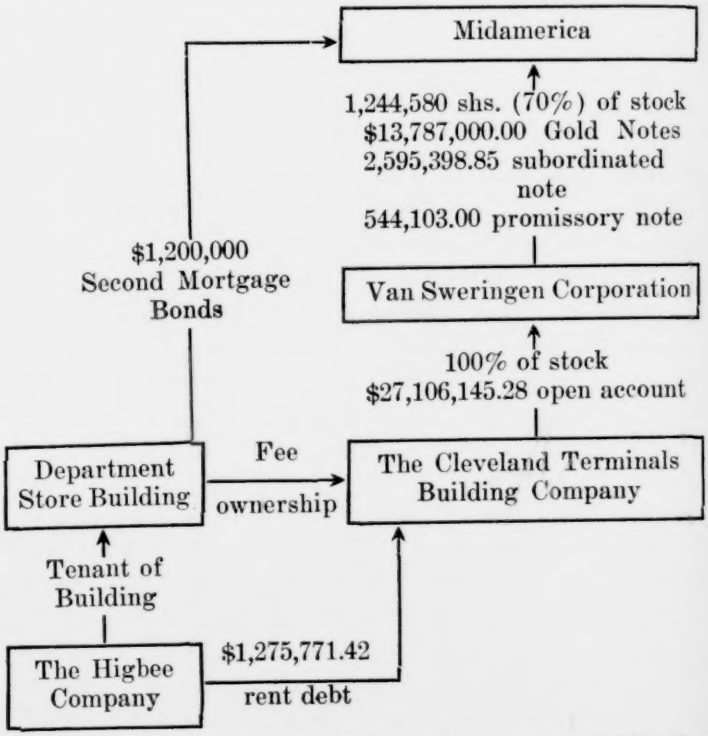
STATEMENT OF THE CASE.

A—Corporate Structure.

During all of the period with which this case is concerned Midamerica was the owner of large claims, direct and indirect, against The Cleveland Terminals Building Company (C.T.B.). These claims were represented by $13,787,000 Van Sweringen Corporation five-year 6% Gold Notes, $2,595,398.85 Van Sweringen Corporation subordinated note, $544,103 Van Sweringen Corporation promissory note and 1,244,580 shares of Van Sweringen Corporation common stock. Van Sweringen Corporation in turn owned all of the capital stock of C.T.B. and a claim against C.T.B. in the amount of $27,106,145.28. Midamerica was also the owner of $1,200,000 principal amount of Second Mortgage 6% Gold Bonds of C.T.B. secured by a second mortgage on the department store building owned by C.T.B. and occupied by Higbee as a tenant (Stip. 29, 30, 31, 32, R. 266-267). C.T.B. in turn was admittedly a creditor of Higbee on notes and for unpaid rent in the amount (as of February 28, 1938) of $1,189,869.93 (Y & K

Ex. 42, R. 458). C.T.B., by proof of claim filed April 22, 1938, claimed that Higbee was indebted to it in the amount of $1,275,771.42 and reserved the right to make a further claim for damages for rejection of leases (Y & K Exs. 39, 40, R. 442-451). C.T.B. also asserted by application that Higbee should affirm or reject the leases which it had entered into with C.T.B. (Y & K Ex. 40, R. 451). Furthermore, Higbee was continuing to occupy the building owned by C.T.B.

For the sake of clarity the relationships of the various individuals and corporations may be set forth graphically as follows:



Bradley was Vice President and a director and Murphy was secretary of Midamerica. Bradley was Vice President

and a director and Murphy was Secretary and a director of Van Sweringen Corporation. Bradley was President and a director and Murphy was Secretary and a director of C.T.B. These relationships continued until January 19, 1938 (R. 289).

B—The Wrongful Purchase.

On September 30, 1935 J. P. Morgan & Co. sold at foreclosure sale large blocks of securities formerly owned or controlled by the Van Sweringen brothers. George Ball of Muncie, Indiana, with an associate, caused the organization of Midamerica for the purpose of bidding at the sale. He was successful in the venture as Midamerica was the high bidder, acquiring for $3,121,000 large blocks of Alleghany Corporation common and preferred stock, certain Cleveland real estate securities including the claims against Van Sweringen Corporation and C.T.B. mentioned above, the Higbee securities which are the subject of this litigation and certain other miscellaneous items. The Van Sweringen brothers were associated with Ball, and were active in the management of the enterprise.

Bradley immediately became Vice-President and a Director of Midamerica and Murphy, its Secretary and counsel. Thus from the very organization of the corporation they acquired intimate knowledge of its affairs.

On April 24, 1937 (the Van Sweringen brothers having died in the interim) Robert R. Young, Allan P. Kirby and Frank F. Kolbe purchased from Ball Foundation 93.67% of the common stock of Midamerica together with substantial blocks of Alleghany securities, pursuant to a contract of sale (R. 44). The purchase price was $6,375,000 of which $4,000,000 was paid in cash and the balance represented by a promissory note. The Higbee securities had been eliminated from the Midamerica portfolio prior to the sale of the Midamerica stock pursuant to a provision in the contract of sale.

On May 15th, 1937, Bradley and Murphy, without notice to the majority stockholders of Midamerica or even to its board of directors, entered into an agreement with Ball Foundation to buy the Higbee securities which are the subject of this litigation and which represent control of the Higbee Company (R. 315-316). The agreement of May 15th was consummated on June 4th by the execution of a bill of sale by Ball Foundation to Bradley and Murphy, the making of a $60,000 cash payment by Bradley and Murphy on account of the purchase price, and the delivery by them to Ball Foundation of their promissory note for $540,000, the balance of the agreed purchase price (R. 19-24).

No claim is made by respondents Bradley and Murphy that they consulted with Midamerica, its Board of Directors or its new owners before this purchase was made. In fact they admittedly acted surreptitiously and concealed their intentions and their negotiations from Midamerica and its new owners until after their arrangements for purchase had been concluded (R. 167).

Midamerica's principal asset was its interest in downtown Cleveland real estate and included a substantial equity interest in the department store building owned by C.T.B. and occupied by The Higbee Company as a tenant as well as a second mortgage in the amount of $1,200,000 on that building. On May 12 and 13, 1937 the new owners, Young, Kirby and Kolbe made their first visit after the purchase to see their new properties in Cleveland.

During those two days they physically inspected all of the properties. Bradley personally escorted them through the Higbee store and pointed out its many advantages and features. They then sat down with balance sheets, income statements and all the financial data which was necessary to a complete understanding of the situation. Bradley's own testimony concerning this occasion is illuminating as

it shows the activities and mental attitudes of all parties concerned at that time (R. 249-250):

"Q. During the course of the inspection tour did you take them through the Higbee store?

A. I think we did.

Q. Do you remember that you went through about every floor of the store?

A. I don't recall that, but we may have.

Q. And that you went up to a radio station on the top floor?

A. We may have done that. Probably did.

Q. That you went into the beauty parlor?

A. We probably did.

Q. And that you pointed out to these gentlemen that it was the very largest beauty department in the city with fifty operators?

A. Well, I don't think I did that because we had more operators. What I said to them was, I think, that it was the second largest in the country. We had better be accurate.

Q. So that you did take Mr. Young, Mr. Kirby and Mr. Kolbe through the Higbee store and they went through the whole place?

A. Yes, sir. They had an interest in the Higbee situation.

Q. Yes. Now, what interest did they have in the Higbee situation, that you discussed with them?

A. I thought at that time they had a very large interest in the Cleveland Terminals Building Company, and they did, too, and the Cleveland Terminals Building Company had a second mortgage, and before they bought into the picture the Cleveland Terminals Building Company had gone into reorganization, and a plan was then being prepared for the reorganization of the Cleveland Terminals Building Company, and a large amount of time, weeks had been spent on it, and months of work had been spent on it, and that second mortgage was being treated in that plan, and I wanted them to know all about it.

Q. Now, you explained all that to Mr. Young and Mr. Kirby?

A. Yes; and to their lawyers.

Q. Yes. You told them of the fact that the second mortgage was for $1,200,000?

A. I told them all the facts.

Q. Well, that is the fact, isn't it?

A. I think it is. Whatever the facts were I told them.

Q. You told them also about the large first mortgage held by The Metropolitan Life Insurance Company?

A. They had all the facts.

Q. You told them that?

A. Yes.

Q. You told them about the back rent claims that C.T.B. had against Higbee?

A. I am sure they were told all about it.

Q. Did Mr. Young ask you for figures on the sales of Higbee?

A. I think he did.

Q. And you discussed that situation with him?

A. I must have. Probably did.

Q. Mr. Young expressed great interest in the progress of the Higbee store and its business affairs?

A. I wouldn't say that. No more so than he was interested in all the things that he came out to look at.

Q. But he did discuss in detail the first mortgage, the second mortgage, the back rent and the sales of the Higbee store?

A. I am sure those were all discussed, yes."

The interest of Young and Kirby in Higbee as was developed in Bradley's presence on May 13, 1937 was indeed distressing to Bradley and Murphy. The telephone records produced at the trial show that on that very same day, May 13, while Young and Kirby were probably having lunch, Murphy called Ball in Muncie, Indiana, on the long distance telephone. As soon as he had concluded his conversation Bradley called Bernard (Ball's assistant). Immediately thereafter Bradley called Ball (Y & K Exs. 36, 37 and 38, R. 441). Admittedly these calls, made in secrecy, were for the purpose of arranging an appointment in

Muncie on May 15 at which Bradley and Murphy could discuss and negotiate with Ball for the purchase of the Higbee securities. They had not mentioned their intentions to the new controlling stockholders of Midamerica.

Bradley and Murphy admit that, although they were purporting to co-operate with Midamerica (R. 248) and the new purchasers of its stock throughout the months of May and June, no information was given by them or anyone else to the new purchasers concerning the said purchase of the Higbee securities, until Bradley communicated the fact to Young on June 7th (R. 167). Young denies that he was given the information until a later date, but for the purpose of this brief, we need not go beyond the testimony of Bradley and Murphy that the purchase from Ball Foundation was agreed to on May 15th, consummated on June 4th, and concealed from Young and his associates until June 7th.

C—Conflict Created by Bradley-Murphy Purchase.

The Higbee Company was in reorganization proceedings when Bradley and Murphy made this purchase. One of the principal obligations of Higbee was its continuing obligation for the payment of rent. Higbee was thus presented with the question as to whether it should assume or reject its lease from C.T.B. Rejection would give C.T.B. a claim for damages provable under the Bankruptcy Act. Adoption would have required payment forthwith of the amounts specified in the lease. This in itself would have been a serious problem for Higbee. But that is not all. The Higbee lease had undergone certain modifications resulting in a reduction of rent. Higbee, however, had not paid, and was not then paying, the rent as so reduced; thus giving rise to the question as to whether Higbee still had a right to take advantage of the reduction in rental, or whether the original rental had been restored automatically or could be restored at C.T.B.'s option. Bradley frankly

testified that the lease from C.T.B. was burdensome, and that it was necessary to relieve this burden in order that the securities which he and Murphy had acquired would become valuable (R. 318 to 320, 442, 451, 458).

C.T.B., in which Midamerica had such a substantial interest, filed its proof of claim against Higbee (R. 442) claiming $1,275,771.42 as a rent debt and reserved the right to assert further claims for damages for rejection of the lease. C.T.B. also filed an application to require the Debtor to assume or reject its leases (R. 451). Bradley and Murphy, who theretofore were supposed to be looking after the interests of Midamerica, changed sides when they acquired the Higbee securities, and, because their self-interest so dictated, they opposed all efforts of C.T.B. to have its claims allowed and to collect for the use and occupation of the Higbee building (see Y & K Ex. 41, R. 455; Y & K Ex. 42, R. 458). Bradley resisted the claim for rent filed by C.T.B. and there resulted extensive litigation not finally determined until passed upon by the Sixth Circuit Court of Appeals (R. 310).

Thus, serious controversies between C.T.B. as landlord and Higbee as tenant had to be litigated or adjusted, relating to the collection of past rentals, the validity and interpretation of the lease and rental agreement, and the fixing of future rentals (R. 306, 308). Midamerica was a substantial direct creditor of Higbee's landlord, and had even greater indirect interests by way of claims and stock ownership through Van Sweringen Corporation. Yet Bradley, a director and officer, and Murphy, an officer and general counsel, of Midamerica, without notice to the other Midamerica officers and directors or to its stockholders, bought for their own account these securities of the tenant, which could have value only if concessions were made by the landlord. They thus put themselves in such a position that their personal interest would necessarily be in conflict

with the Midamerica interests, which Midamerica officers and directors were duty-bound faithfully to protect.

The position which they assumed was so obviously in conflict with their duties to C.T.B. (Midamerica's subsidiary) that on July 2, 1937, just a few days after the public announcement of the Bradley-Murphy purchase, Honorable Charles I. Russo, Special Master in the C.T.B. reorganization proceedings, recommended the appointment of special counsel for C.T.B. and in his report (Stip. Ex. W, R. 300) he made the following statement:

> *"The relationship of the two Companies arising out of the aforestated acquisition of the stock of The Higbee Company by officers of the Subsidiary Debtor appears plainly to leave no alternative, than to take, for the benefit of creditors of Subsidiary Debtor, such precautionary measures as are necessary to avoid the difficulties so often pointed out by the Courts."* (Italics ours.)

The District Court in approving the Master's recommendations specifically found the conflict which had been created, and appointed disinterested representation for C.T.B. (R. 302-4).

This conflict in Bradley's and Murphy's position was no less grave in respect of Midamerica, whose principal asset was its interest in C.T.B. and particularly the $1,200,000 of C.T.B. bonds secured by a second mortgage on the Higbee building, which mortgage could only be serviced and amortized by rental payments made by Higbee as tenant.

One very important immediate effect of the Bradley-Murphy purchase was to deprive Midamerica of the attention of Bradley to the duties incident to the position he occupied. On June 27, 1938 Murphy testified that Bradley had, since the Bradley-Murphy purchase, "become the President" of Higbee and "devoted a great part of his time, in fact most of it * * * to the affairs of the Higbee Company" (B & M Ex. 7, R. 388). Thus it is apparent

that Bradley was devoting practically all of his time to Higbee and completely disregarding the interests of Midamerica.

It is difficult to conceive of a breach of trust involving a fiduciary in more inconsistent positions. The applicable rule of law was created to prevent the slightest departure from the line of duty to one's master. But here the ensuing waves of conflicting loyalties are so many and involved as to point up the unconscionable nature of Bradley's and Murphy's conduct. Not only did they buy for themselves property desired by their principal, for whom they were acting; not only did they, as part of the price, involve themselves in inevitable future disloyalty; but they placed themselves in the position in which the performance of their duty to the corporation of which they were officers and directors, would injure their personal interest in the securities acquired. They were faced with the constant conflict the law intended must never exist, of serving themselves at the sacrifice of their fiduciary obligations.

On July 15, 1937, Young, having learned of the Higbee purchase, wrote Bradley (Y & K Ex. 27, R. 424) who, with Ball and Bernard, continued to control the Board of Directors of Midamerica (although Young, Kirby and Kolbe owned substantially all of its stock) and asked Bradley to remove the Board of Directors and elect a new board which Young had told him was to be Young, Kirby, Kolbe, McKinney and Ball (R. 171). This request was refused by Bradley.

In August 1937 Mr. Milton A. Kramer, attorney for the Young interests, came to Cleveland and, after having been instructed so to do, he pointed out to Murphy the conflicting position which Murphy and Bradley had assumed by their acquisition of the Higbee securities. He was instructed by Young to take a firm stand with Bradley and Murphy, and pursuant to those instructions he made

known Young's position that Bradley and Murphy had assumed a conflicting position because they were representing the landlord, the second mortgagee and the owner of the equity in C.T.B., the landlord, at the very time they acquired for themselves a controlling interest in Higbee, the tenant (R. 98).

In January, 1938 Bradley and Murphy finally recognized that on May 15, 1937 they had placed themselves in conflict with duties owing to their employers, because they then resigned as directors and officers of C.T.B. and Midamerica (Stip. Ex. U, R. 290-292).

Bradley and Murphy *never* voluntarily disclosed the price and terms of their purchase. On June 27, 1938, more than a year later, and after Midamerica had made formal application therefor, Murphy was examined as a former officer of C.T.B., and was thereupon forced to disclose the details of the deal with Ball (R. 179).

ARGUMENT.

During the year 1937 Bradley and Murphy were executive officers and Bradley a director of Midamerica. Both were executive officers and directors of Higbee's landlord, C.T.B., then in bankruptcy reorganization. Midamerica held a second mortgage on the building owned by C.T.B. and occupied by Higbee under a disputed lease on which substantial rental obligations were in arrears. Midamerica also owned very large claims against C.T.B.

Bradley and Murphy, with full knowledge of this situation, in 1937 secretly purchased controlling interest in Higbee while it was also in bankruptcy reorganization. Shortly after that purchase, Bradley, who already was a director, became president of Higbee. At the same time Murphy became a director. Conflict was inevitable, and it was recognized by the Circuit Court. We quote from the opinion in this case:

> "If C.T.B. had any substantial interest in this matter * * * we think that a substantial conflict of interest would have been created between the parties" (R. 566).

The court undertook, however, to measure the amount of C.T.B.'s interest in opposition to Higbee, and apparently to weigh it against the value of the interest which Bradley and Murphy had acquired. Having done so it concluded that the interest of C.T.B. was not sufficiently substantial to warrant the imposition of a constructive trust on the Higbee securities. This action by the Circuit Court was in error for the following reasons:

1. To measure the quantum of interest is a departure from sound judicial practice and is neither within the capacity nor the scope of a court's purview in deciding a case.

Judge Cardozo said, in *Meinhard vs. Salmon,* (commented on below):

> "No answer is it to say that the chance would have been of little value even if seasonably offered. Such a calculus of probabilities is beyond the science of the chancery."

2. The Circuit Court's conclusion that the interest of C.T.B. in Higbee was not substantial in 1937 was contrary to what all parties believed at that time (R. 249). It was based upon the decision by the same court rendered in 1939 in *The Higbee Company vs. The Cleveland Terminals Building Company,* 106 F. (2d) 796. The decision in the instant case has the effect of antedating the judgment in the C.T.B. case from 1939 to 1937.

Substantial Interest.

The Circuit Court found that, but for circumstances discussed below, "a substantial conflict of interest would have been created between the parties," that is, between Midamerica on the one hand and Bradley and Murphy

on the other. The court thus recognized that a conflict of interest was inherent in the situation. The court, however, refused to impress a trust on the Higbee securities largely because it was of the opinion that Midamerica's interest in Higbee was not substantial.

Courts of equity have not heretofore attempted to weigh or appraise the extent of a litigant's interest in a subject concerning which there is an admitted conflict. So long as Midamerica had any interest in the Higbee situation, whether great or small, then the admitted conflict was objectionable and the fiduciary relationship of Bradley and Murphy to the corporation must be recognized by holding them accountable for their purchase at the election of Midamerica.

The well-known case of *Meinhard vs. Salmon*, 249 N. Y., 458, deals with this very point. In that case Meinhard and Salmon were joint adventurers in a lease of property in New York City. Meinhard advanced the money and Salmon operated the business. The profits were divided. Shortly before the expiration of the lease Salmon, for himself alone, negotiated a new lease covering the same property originally leased and a large adjacent parcel. The new lease was different from the old one in that it required the erection of a building covering the entire leased premises and involved a much larger rent than required under the original lease. Meinhard had no knowledge of this situation until after Salmon had entered into the new lease. The court, speaking through Judge Cardozo, impressed a constructive trust on the new lease for the benefit of Meinhard.

Salmon contended that the original venture was about to end and that there was no obligation for the partnership to continue. The court agreed with that, but found that Meinhard was entitled to a chance to compete with Salmon for the new lease. Obviously that chance was of doubtful monetary value. Quite evidently Meinhard's in-

terest in the situation was not substantial. Nevertheless, the court there held it is no defense to Salmon because Meinhard's chance was of little value and that the court could not weigh the value of Meinhard's chance. We quote from Judge Cardozo's opinion:

> "The pre-emptive privilege, or, better, the pre-emptive opportunity, that was thus an incident of the enterprise, Salmon appropriated to himself in secrecy and silence. He might have warned Meinhard that the plan had been submitted, and that either would be free to compete for the award. If he had done this, we do not need to say whether he would have been under a duty, if successful in the competition, to hold the lease so acquired for the benefit of a venture then about to end, and thus prolong by indirection its responsibilities and duties. The trouble about his conduct is that he excluded his coadventurer from any chance to compete, from any chance to enjoy the opportunity for benefit that had come to him alone by virtue of his agency. This chance, if nothing more, he was under a duty to concede. The price of its denial is an extension of the trust at the option and for the benefit of the one whom he excluded.
>
> No answer is it to say that the chance would have been of little value even if seasonably offered. Such a calculus of probabilities is beyond the science of the chancery."

The final paragraph of the above quotation expresses in superb language our view on this point. In 1937 Midamerica was asserting large claims against C.T.B., one of which, in the amount of $1,200,000, was secured by a second mortgage on the building occupied by Higbee as tenant. C.T.B. in turn was asserting large rental claims against Higbee under a disputed lease. The ultimate value of those claims could not at that time be predicted; it depended, of course, largely on the outcome of litigation then pending and then being initiated, in which the officers of Midamerica were in duty bound to maintain undivided loyalty to the corporation.

Another case in which the court brushed aside the plea of a faithless fiduciary that no substantial interest was involved is that of *Irving Trust Co. vs. Deutsch*, 73 F. (2d) 121. This case, decided by the Second Circuit Court of Appeals in 1934, announces the rule of strict accountability of fiduciaries and allows no exceptions to that rule. The decision of the Sixth Circuit Court in the instant case relieving Bradley and Murphy of their obligation to account to Midamerica for their purchase of the Higbee securities, because Midamerica's interest in Higbee was "not substantial" is thus directly in conflict with the decision of the Second Circuit Court.

The facts in the *Irving Trust* case are that former officers of Acoustic Corporation, a bankrupt, had taken advantage of a contract which the trustee in bankruptcy claimed should have been given to the corporation. We quote from the court's opinion.

> "The defendants' argument, contrary to *Wing v. Dillingham*, that the equitable rule that fiduciaries should not be permitted to assume a position in which their individual interests might be in conflict with those of the corporation can have no application where the corporation is unable to undertake the venture, is not convincing. If directors are permitted to justify their conduct on such a theory, there will be a temptation to refrain from exerting their strongest efforts on behalf of the corporation since, if it does not meet the obligations, an opportunity of profit will be open to them personally.
>
> * * * * *
>
> If the directors are uncertain whether the corporation can make the necessary outlays, they need not embark it upon the venture; if they do, they may not substitute themselves for the corporation any place along the line and divert possible benefits into their own pockets. 'Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the "disintegrat-

> ing erosion'' of particular exceptions.' *Meinhard v. Salmon,* 249 N. Y. 458, 464, 164 N. E. 545, 546, 62 A. L. R. 1.''

In the *Irving Trust* case the court recognized the danger of allowing a particular exception to the rule of fiduciary responsibility because a corporation may not have the means to take advantage of its rights. In that case Acoustic Corporation's interest in the contract, because of its lack of funds, was of doubtful monetary value, and could not have been substantial. Clearly the decision turned, not on the extent of Acoustic Corporation's interest, but on the fact that it had any right or interest in the subject.

The rule of the Second Circuit Court was followed without limitation in the recent case, *In re Standard Commercial Tobacco Co.,* 34 Fed. Supp. 304. That decision was by the District Court for the Southern District of New York in 1940. In its opinion the court quoting from Lord Eldon *Ex Parte James* 8 Ves., said:

> '' 'The purchase is not permitted in any case, however honest the circumstances; the general interests of justice requiring it to be destroyed in every instance; as no court is equal to the examination and ascertainment of the truth in much the greater number of cases.' ''

We thus see that, since Lord Eldon's time, once the conflict is established, the circumstances, no matter how honest, cannot alter the fiduciary's obligation. Whether Midamerica's interest in the Higbee securities later turned out to be substantial or only nominal makes no difference in the application of the rule of accountability by Bradley and Murphy as fiduciaries.

Antedating a Judgment.

In the Circuit Court's opinion in the instant case, the Court referred to its decision in 1939 in the suit brought by C.T.B. against Higbee for rent claims. There the Court held in substance that the large claims asserted by C.T.B. were only enforceable in part. We quote from the opinion in the instant case:

> "This court, in *Higbee Co. v. Cleveland Terminals Building Co.*, 106 Fed. (2d) 796, 799, 800, held that the trustee thus became the real party in interest and the beneficial owner of notes aggregating more than $570,000, for rent due from the lessee. The Cleveland Terminals Building Company had only a nominal interest in the building, * * *." (R. 567.)

(In passing we point out that as owner of the second mortgage Midamerica had an interest in the building which was prior to that of C.T.B.)

It appears that the Circuit Court regarded the instant case as a challenge to the correctness of its decision in the C.T.B. rent case. The Court evidently felt it necessary, in order now to sustain its decision in 1939, to find in this case that at a time two years earlier, namely on May 15, 1937, Midamerica's interest in the Higbee situation was but nominal.

We do not here question the correctness of the Circuit Court's decision in the C.T.B. case. However, that case dealt only with C. T. B.'s right to collect certain rent claims from Higbee; C.T.B.'s interest in the Higbee building was not one of the issues to be decided. The important point is that the decision, whether it went beyond the scope of the question before the Court or not, was rendered in 1939.

In 1937, everyone connected with the situation thought that C.T.B.'s interest in Higbee was very substantial. (R. 249.) Its rent claim which certainly was a debatable question was for $1,275,771.42. Since no one could know in 1937 the final outcome of litigation which was to end in 1939,

Bradley and Murphy in the instant case cannot now be absolved from their fiduciary obligations to Midamerica which existed in 1937, because of a decision in a case to which Midamerica was not a party, rendered in 1939.

Because of the unforeseen outcome of the C.T.B. case, in which Bradley and Murphy, after their purchase of the Higbee securities, gave their efforts in favor of Higbee and against the rights of C.T.B. and Midamerica, we now find them doubly rewarded for assuming a position in which they could not faithfully serve both masters. First, Higbee gained at the expense of C.T.B. and Midamerica. Second, by force of the C.T.B. decision in 1939, Bradley and Murphy were excused from accounting for their violation of fiduciary duty in purchasing the Higbee securities in 1937. If the present decision of the Circuit Court is permitted to stand, we have at last found the case where two wrongs make a right.

The decision of the Circuit Court in the instant case has the effect of rendering a *nunc pro tunc* judgment in *Higbee Co. v. C.T.B.*, antedating that decision from 1939 to 1937. Courts only resort to *nunc pro tunc* entries to correct an error or to prevent a miscarriage of justice. In this case, to antedate the effect of the C.T.B. decision that Midamerica's interest in 1939 in the Higbee situation was not substantial, serves to reward fiduciaries for their faithlessness.

Estoppel.

The Circuit Court held that Midamerica was estopped to assert its equitable claim against Bradley and Murphy. We quote from the Court's opinion:

> "On June 3, 1942, before the hearing in this proceeding began, Midamerica notified Bradley and Murphy that it would accept payment of the note, and Bradley and Murphy again borrowed the necessary sum and paid in open court the amount of $566,290.36 * * *. Thus

Midamerica placed itself in a position sharply inconsistent with the position which it now asserts. If Bradley and Murphy were obliged to pay the note, then their purchase was valid and they have both legal and equitable title to the securities. By its demand for payment, Midamerica acquiesced in the transaction and recognized the rights of Bradley and Murphy." (R. 567, 568.)

It is evident that the Circuit Court never understood Midamerica's position in this matter. We have always contended that Bradley and Murphy acquired legal title to the securities from Ball Foundation. There was a financial encumbrance on that title in the note which Bradley and Murphy signed in favor of Ball Foundation, to which the Higbee securities were attached as collateral. In an entirely independent transaction resulting from the settlement of litigation between Ball Foundation and Young and Kirby, the Bradley and Murphy note and the accompanying collateral were transferred to Midamerica. The transfer was an incident in the course of business between other parties and involved no relations between Midamerica and Bradley and Murphy.

Bradley and Murphy claimed that they suffered a detriment in paying their note because as a preliminary step, they had borrowed money to make the payment. As a prerequisite to borrowing on the Higbee securities as collateral, they had paid $115,000 to procure the dismissal of an appeal in the Higbee reorganization proceedings then pending in the Sixth Circuit Court, wherein the reorganization plan as approved by the District Court had been objected to by certain preferred stockholders on the ground that Bradley and Murphy as owners of the Higbee securities herein questioned, were to be given too large a share at the expense of the preferred stockholders.

Thus to enable themselves, at one stroke, to remove the threat that the Higbee reorganization plan, favorable to

Bradley and Murphy as then drafted, might be upset, and at the same time to remove the danger that their Higbee securities, which were collateral to their long past due note, might be foreclosed, Bradley and Murphy thought it desirable to buy the pending appeal and cause its dismissal. Their decision to take this step was based upon their own judgment.

The price they paid to buy the preferred stockholders' appeal was about $100,000 above the then market value of the preferred stock which they acquired. This transaction is the subject of other litigation wherein the preferred stockholders, J. F. Potts and William Boag, have been asked to turn over the profit they made above the market value of their securities to the preferred stockholders as a class. The Sixth Circuit Court of Appeals affirmed the District Court in holding that Potts and Boag need not account for their unconscionable profit. (142 F. (2d) 1004.) Petition for writ of certiorari was filed in that case which bears No. 342 on the Supreme Court docket and is now pending decision.

On March 2, 1942, Bradley and Murphy borrowed money to pay the note and tendered it to Midamerica as they had a right to do. For reasons concerning the details of the tender, which are not pertinent here, the tender was refused. Three months later Midamerica accepted Bradley and Murphy's payment of the note without additional interest for the time subsequent to the original tender.

Midamerica had no choice about the matter. It was obliged to accept a valid tender under penalty of losing all interest on a very large sum of money pending the final outcome of this litigation. However, the effect of the payment of the note in no way changed the equitable rights of Midamerica against Bradley and Murphy for their misconduct in purchasing the Higbee securities. By borrowing the money and paying the note, Bradley and Murphy merely paid a pre-existing debt by substituting one creditor for another.

The corporation now has the equitable right under the doctrine of constructive trust to elect to require Bradley and Murphy, upon proper reimbursement, to transfer their legal title to Midamerica. In 1942, Midamerica, through the happenstance of a settlement of other litigation, came to be the holder of an encumbrance against Bradley and Murphy's legal title, which it was obliged to deliver to them upon tender of payment. Midamerica did not thereby impose any new obligation on Bradley and Murphy.

Midamerica has in no manner recognized any equitable interest to the Higbee securities in Bradley and Murphy. On the contrary, it has continuously and vigorously asserted that equitable title to the securities is exclusively in Midamerica.

Our equitable claim has always been subject to reimbursement to Bradley and Murphy of all their legitimate costs, including of course, the payment made to Midamerica itself. Bradley and Murphy suffered no legal or equitable detriment when they paid in full a past due obligation voluntarily assumed by them. If equity should later compel them to give up the securities which they were disqualified by their fiduciary relationship to acquire, equity will also decree full reimbursement to them of legitimate costs, under the rule of *Ashman v. Miller,* 101 F. (2d) 85, and they will still suffer no detriment. In the absence of detriment to Bradley and Murphy a necessary element of estoppel is lacking.

Laches.

The Circuit Court agreed with the conclusion of the Special Master (R. 506) and the District Judge (R. 526) that the statute of limitations does not bar this claim, but overruled the District Court in holding that laches existed irrespective of the statute of limitations.

When the purchase was made from the Ball Foundation in 1937, Bradley and Murphy paid down $60,000 and

signed a note for $540,000. No substantial payment was made on the principal of that note until it was paid off in full as recited above. The terms of the note specifically limited the liability of Bradley and Murphy to the value of the Higbee securities which were attached to the note as collateral. During the four years that elapsed before this litigation was commenced, proper compensation was awarded by the bankruptcy court to Bradley and all others who rendered services of value to the Higbee Company.

However, the most important facts regarding the question of laches were the rulings of the Special Master and the District Court during the course of the reorganization proceedings, that the plan of reorganization should first be worked out and agreed upon and that determination of the several claims to ownership of the Higbee securities should be deferred until the reorganization plan might be approved.

On March 2, 1939, the Special Master filed his memorandum in respect of a motion made by Bradley and Murphy (Y. & K. Ex. 29, R. 426), holding, in part, as follows:

> "The primary purpose of this proceeding is to reorganize The Higbee Company and the Debtor admits, as apparently do all parties herein, that The Higbee Company received the money evidenced by this note and has this debt to be reckoned with in any plan of reorganization. So it would seem the first thing to be done is to adopt a plan of reorganization which would include this claim. Then, at some later hearing it could be determined who is the actual beneficial owner of the claim recognized in the plan of reorganization. Whatever stock, securities or money would go to this claim would be set up in the plan and the determination as to who should receive it could later be made. That is to say, the Court at this time is more interested in a feasible plan and its adoption by creditors than it is in who is to receive a particular share in the plan."

* * * * *

"However, the Master is of the view that at this time the best interests of the Debtor will be served, and progress made in the reorganization proceedings by postponing any action by this Court which goes to the determining of the ownership of this note. As indicated before, the Master is now interested in proceeding with a plan of reorganization and devoting the Court's time and counsel's time to the consideration of a plan and hearings upon questions which must necessarily be disposed of first. When the plan has been approved this question of ownership, if it still exists, will be disposed of either by the Court exercising its discretion to retain jurisdiction of this claim or refusing to hear it."

The plan of reorganization also defers the determination of the ownership of these securities in compliance with the policy expressed by the Special Master in his opinion of March 2, 1939 (R. 361). Reference to this subject was made in the plan because in 1938 opposing claims for the equitable title to the Higbee securities were filed in the reorganization proceedings. When Midamerica's claim was filed it had the effect only of adding a new name to the list of claimants. Midamerica's claim did not originate a contest against Bradley and Murphy.

On June 12, 1941, the Special Master again recognized this policy when he deferred action on the application of Young and Kirby for leave to file proof of claim pending the completion of proceedings on the plan (R. 51).

Bradley and Murphy did not take any exception to the Master's orders, and were even insistent that the matter be delayed for a year after the Young-Kirby claims were filed while the plan was being confirmed. On this delay the District Judge said in his opinion of May 5, 1942:

"The object and purpose of this stay and adjournment of hearing was to avoid any impairment or delay in bringing about a conclusion of the Higbee reorganization."

* * * * *

*

> "The bar order of October 6, 1939, clearly was for the purpose, as the Master said in his report, of determining the persons who were to have the right to vote on the plan. *All questions as to the ownership of the junior indebtedness were to be postponed* under an escrow agreement between the then claimants, dated June 4, 1937. Thus, the bar order was not to affect the question of the right to ownership of the junior indebtedness." (Emphasis added.) (R. 87.)

Midamerica was thoroughly justified in relying upon the numerous orders of the District Court to which Bradley and Murphy fully acquiesced from the beginning. For the Circuit Court now to rule that a claimant in the Higbee reorganization proceedings is guilty of laches because it relied upon the specific orders of the Master and the District Judge relating to the very question before the court, penalizes Midamerica most unfairly.

During the trial of the instant case before the Master, Bradley and Murphy claimed that Midamerica was guilty of laches. The Master found that there were no laches (R. 506). No exception was taken to that finding. All findings of the Special Master were confirmed by the District Court (R. 526) and again no exception was taken by appellees. Bradley and Murphy filed no appeal proceedings in the Circuit Court and asked for no relief against any order of the Master or the District Court. Midamerica did not raise the question of laches. That subject was not before the Circuit Court. Its ruling thereon is clearly beyond the questions presented in the case it decided.

By deciding that Midamerica's interest in the Higbee securities is barred by laches, the Circuit Court has adopted a new procedural technique heretofore unknown to federal practice. 28 U. S. C. A. Sec. 862, dealing with the previous practice of filing writ of error to an appellate court, provides that an assignment of errors shall be included in the writ of error. By virtue of 28 U. S. C. A. Sec. 861a, writ of error was abolished in 1928 and thereafter litigants com-

plaining of the trial court were granted relief by appeal.

Under 28 U. S. C. A. Sec. 861b, we find that the procedure under the former practice of writ of error shall be applicable to the appeal.*

In the modern practice of the Federal Rules of Civil Procedure adopted by the Supreme Court, pursuant to Act of June 19, 1934, we find that in lieu of assignments of error, if the appellant does not designate for inclusion the complete record, he shall, as in this case, serve with his designation a concise statement of the points on which he intends to rely on his appeal. This is provided for in Rule 75 (d) of the District Courts of the United States of the Rules of Civil Procedure just referred to. Rule 75 (d) is as follows:

> "Statement of Points. If the appellant does not designate for inclusion the complete record and all the proceedings and evidence in the action, he shall serve with his designation a concise statement of the points on which he intends to rely on the appeal."

Midamerica filed its statement of points (R. 540). There is no reference in that statement of points to the subject of laches. We quote the first paragraph of Rule 10 of the Sixth Circuit Court of Appeals:

---

* 861a. **Writ of error abolished; substitution of appeal.**—The writ of error in cases, civil and criminal, is abolished. All relief which heretofore (January 31, 1928) could be obtained by writ of error shall hereafter be obtainable by appeal.

861b. **Statutes governing writs of error to apply to appeals.**—The statutes regulating the right to a writ of error, defining the relief which may be had thereon, and prescribing the mode of exercising that right and of invoking such relief, including the provisions relating to costs, supersedeas, and mandate, shall be applicable to the appeal which the preceding section (861a of this title) substitutes for a writ of error.

862. **Removal of causes by former writ of error.**—There shall be annexed to and returned with any writ of error for the removal of a cause, at the day and place therein mentioned, an authenticated transcript of the record, an assignment of errors, and a prayer for reversal, with a citation to the adverse party.

"10. Appeals in Civil Actions.—1. Federal Rules of Civil Procedure adopted by the Supreme Court pursuant to Act of June 19, 1934, Nos. 73, 74, 75 and 76, are adopted as rules of this court in cases to which they may apply."

Clearly laches was not a question for consideration by the Court of Appeals. So far as the decision was based on that point, it involves a departure from the court's own rules and from the Federal Rules of Civil Procedure adopted by the Supreme Court. Moreover, there is no merit to appellees' defense of laches because of the several rulings of the Master and the District Judge, which deferred any consideration by the District Court of the pending claims to equitable ownership of the Higbee securities.

CONCLUSION.

In the petition for the writ of certiorari preceding this brief, we have presented three questions that definitely bring this case within Supreme Court Rule 38 paragraph 5 (b).

1. The decision of the Sixth Circuit Court of Appeals is in conflict with the decision of the Second Circuit Court of Appeals in the case of *Irving Trust Co. vs. Deutsch,* 73 F. (2d) 121.

2. The judgment complained of has decided important federal questions regarding the administration of bankruptcy reorganizations which have not been, and should be, settled by the Supreme Court.

3. In antedating the effect of its judgment in the C.T.B. rent case, 106 F. (2d) 796, and in introducing the element of laches which was not presented in the appeal, the Sixth Circuit Court has so far departed from the accepted and usual course of judicial procedure as to call for an exercise of the Supreme Court's power of supervision.

In view of the foregoing we request the Supreme Court to grant the petition for writ of certiorari.

Respectfully submitted,

ROBERT J. BULKLEY,
JAMES A. BUTLER,
ROBERT W. PURCELL,
Attorneys for the Terminal and Shaker Heights Realty Co.

(20)

In the Supreme Court of the United States

OCTOBER TERM A. D. 1944.

No. 496.

THE TERMINAL AND SHAKER HEIGHTS REALTY COMPANY,
Petitioner,

vs.

CHARLES L. BRADLEY and JOHN P. MURPHY,
Respondents.

BRIEF OF RESPONDENTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

CHARLES K. ARTER,
LEWARD C. WYKOFF,
2800 Terminal Tower,
Cleveland 13, Ohio,
Attorneys for Charles L. Bradley and John P. Murphy.

THE GATES LEGAL PUBLISHING CO., CLEVELAND, OHIO—MAIN 5647

INDEX.

AUTHORITIES CITED.

Cases Cited or Distinguished.

In the Supreme Court of the United States

OCTOBER TERM A. D. 1944.

No. 496.

THE TERMINAL AND SHAKER HEIGHTS REALTY COMPANY,
Petitioner,

vs.

CHARLES L. BRADLEY and JOHN P. MURPHY,
Respondents.

BRIEF OF RESPONDENTS.

RESPONDENTS' POSITION.

This case presents no question of law concerning which there is any conflict of authority, any lack of uniformity of decision between the different circuit courts of appeals, nor does it involve a single principle of law the soundness of which is disputed by the adverse parties.

The facts were complicated; they were largely based on conflicting oral testimony, on the credibility of witnesses, most of whom were interested, and on inferences to be drawn from a multitude of documents. The Special Master, with painstaking care, sifted the evidence and, by an exhaustive report, made what the Circuit Court of Appeals referred to as "extended" [1] findings of fact. These findings of fact were adopted by the District Court, with certain additional findings of its own, and all was confirmed by the Circuit Court of Appeals.

It is here stated by the respondents, with confidence and without reservation, that the facts, as found by the

[1] R. 562.

tribunals below, present no question either of public interest or of general law about which there is or can be a dispute.

The "Statement of the Case," beginning on page 7 of petitioner's brief, is not based on the facts as found by the courts below, but rather on assertions, in many instances not supported by the record, and, in others, upon testimony rejected by the courts below as having no probative value. Petitioner now seeks a reexamination of the evidence, the weight and effect of which have three times been found against it.

Respondents' Statement of the Case herein is based upon the findings of the courts below (all of which are ignored in petitioner's brief) and these findings will themselves demonstrate the soundness of respondents' position.

STATEMENT OF THE CASE.

(1) The Fiduciary Relationship.

Midamerica was the owner of the Higbee securities, which are the subject of this controversy. (F.* 1, R. 492.) Bradley and Murphy began their negotiations with Midamerica to purchase its holdings of Higbee securities in January 1937. (F. 2, R. 492.) These negotiations were carried on with Mr. Ball, who, at that time, was a director of Midamerica, and its sole stockholder. (F. 1 and 2, R. 492, F. 6, R. 493, R. 289.) Mr. Ball, during these negotiations, donated his Midamerica stock to the Ball Foundation. (R. 466.) (Hereinafter both Mr. Ball and the Ball Foundation will be referred to as the Ball Foundation.) The Ball Foundation, on May 5, 1937, sold to Robert Young and associates (hereinafter referred to as the Young syndicate) the common stock of Midamerica. (F. 7, R. 494.) At the beginning of the negotiations with the Young Syndi-

---

* Explanation of abbreviations:

F.—Findings of Special Master.
Br.—Petitioner's Brief.
R.—Record.

cate, it was disclosed and understood that the Higbee securities, then owned by Midamerica, were being held for sale to Bradley and Murphy and therefore excluded from the Young negotiations. (F. 3, R. 493.) In accordance with and pursuant to this understanding, Midamerica, by means of a partial liquidation of its assets, distributed the Higbee securities to the Ball Foundation on May 4, 1937,—one day before the purchase of Midamerica's common stock by the Young Syndicate from the Ball Foundation. (F. 6, R. 493.) At the time when the Young Syndicate purchased Midamerica, Bradley and Murphy had practically concluded negotiating for Midamerica holdings of Higbee's securities. (Finding of the District Judge No. 5, R. 529.) Ten days later, on May 15, 1937, Bradley and Murphy concluded their negotiations and purchased the Higbee securities. (F. 11, R. 495.)

Petitioner contends that this purchase by Bradley and Murphy created a conflict of interest between the duty Bradley and Murphy owed to Midamerica and their personal interest as owners of the Higbee securities.

Bradley and Murphy were officers of Midamerica and Bradley was a director at the time they purchased the Higbee securities. (F. 10, R. 494.)

Midamerica had nothing but a nominal interest in The Cleveland Terminals Building Company on May 15th, 1937 (F. 29, R. 498); and The Cleveland Terminals Building Company, although the holder of the legal title to the building occupied by The Higbee Company, had no equity in the building. The real owner of the building, together with the lease and rentals, was The Metropolitan Life Insurance Company (F. 32, R. 498),—not a party to, or concerned in, this litigation.

No negotiations were had between Higbee and The Cleveland Terminals Building Company with respect to any rental relationships involving The Higbee Company at a time when Bradley or Murphy were either directors

or officers of Midamerica. (R. 307-8.) Quite obviously there was no occasion for such negotiations during 1937, since the contract of 1935 between Higbee Company and The Cleveland Terminals Building Company fixed the rental relationship until March of 1940. (106 F. 2d 796, 797, 798, by stipulation made a part of this record, R. 215.)

(2) Estoppel.

At the time when they purchased the Higbee securities in 1937, Bradley and Murphy gave to the Ball Foundation, in partial payment for such purchase, their personal note for $540,000 secured by the Higbee securities. (F. 11, R. 495.) Midamerica, on March 2, 1942, acquired from the Ball Foundation this note together with the collateral pledged as security therefor including the Higbee securities. (F. 41, R. 500.) The following day Midamerica declared it due, and notified Bradley and Murphy of its intention to sell the collateral (consisting of the Higbee securities) at public sale on March 13, 1942, and reserved its right to bid at the sale. (F. 44, R. 501.) The note by its terms provided that the holder thereof need not account to the makers for any overplus received at the sale; thereby, in effect, prohibiting any other bidder from bidding in competition with Midamerica, thus enabling Midamerica, without cost, to acquire the Bradley-Murphy holdings, leaving in them no equity of redemption. (R. 23.)

Midamerica, at the time it served said notice, had knowledge of all facts relative to the rights it was asserting in these proceedings, and intended that the position which it took would be acted upon by Bradley and Murphy. (F. 45, R. 501.)

Bradley and Murphy did act upon said notice and changed their position for the worse (F. 46, R. 501); and among other things (F. 50, F. 51, F. 52, R. 502, F. 55, R. 503) borrowed $560,000 and paid the same to Midamerica in full payment of said note. Midamerica thereupon sur-

rendered to Bradley and Murphy the cancelled note and all collateral described therein consisting of the Higbee securities. (F. 57, R. 503.)

(3) Laches.

Although Bradley and Murphy concluded their purchase of the Higbee securities on June 4, 1937 (F. 11, R. 495), and although Bradley notified Young and Kirby of the purchase on June 7, 1937 (F. 12, R. 495) and although public announcement of the purchase was made in Cleveland and New York newspapers on June 28, 1937 (F. 13, R. 495) and although Bradley and Murphy thereafter devoted their time and efforts to the affairs of The Higbee Company in the management of its store business and the development of a Plan of Reorganization acceptable to its creditors (F. 14, R. 495), and although the affairs of The Higbee Company during the administration of Bradley and Murphy improved greatly (F. 15, R. 495), Midamerica did not at any time until March 28, 1942, more than four years later, assert that purchase of the Higbee securities by Bradley and Murphy was a violation of any fiduciary duty which Bradley and Murphy owed to Midamerica. (F. 35, R. 499.) As stated in the opinion of the Circuit Court of Appeals:

> "In fact the entire record shows by convincing evidence that not until after The Higbee Company had become a very profitable enterprise was the present claim asserted." (R. 564.)

ARGUMENT.

The petitioner contends:

1. Error was committed by the Circuit Court of Appeals in failing to find that a conflict of interest was created by the purchase by Bradley and Murphy of the Higbee securities.

2. Error was committed by the Circuit Court of Appeals in its determination that the claim of the petitioner is barred by estoppel.
3. Error was committed by the Circuit Court of Appeals in its determination that the claim of the petitioner is barred by laches.

Conflict of Interest.

The facts upon which petitioner relies consist, in the main, either of unwarranted inferences or of testimony rejected by the Special Master and by him found to be discredited. The report of the Master was approved and adopted by the District Court, which in turn was affirmed by the Circuit Court of Appeals.

The Special Master found that Midamerica *never had** more than a nominal interest in The Cleveland Terminals Building Company (F. 29, R. 498), and The Cleveland Terminals Building Company in turn had no equity in the building occupied by The Higbee Company. (F. 32, R. 498, 499.) Hence nothing which Bradley and Murphy could do could possibly have affected Midamerica.

It is nothing short of pure sophistry to argue that even though Midamerica's claims were allowed by the Court for nominal amounts only, they should nevertheless be considered, for the purposes of this controversy, as representing a real interest, because Midamerica asserted them for their face amounts. It follows that petitioner's argument, that the Circuit Court of Appeals treated its determination of Midamerica's claims against The Cleveland Terminals Building Company as a *nunc pro tunc* adjudication, is equally unwarranted. When the Circuit Court of Appeals allowed these claims for nominal amounts it determined judicially that, in the hands of Midamerica, they *never* represented more than a nominal interest.

---

* Emphasis throughout that of respondents.

As the same Court held in *Ashman v. Miller,* 101 F. 2d 85, relied upon by petitioners, it is when, and only when, a damage might result to the interest of the corporation from the relationship which its directors had assumed, that a fiduciary duty is involved. Of course, if the corporation has no interest, then a non-existent interest could not be damaged.

There never was a time, after Bradley and Murphy became the owners of the Higbee securities, when there was *even a possibility* that Midamerica could be damaged by anything which Bradley and Murphy could do as the owners of the Higbee securities.

The undisputed evidence and the findings of the courts below disclose that, if the inference be indulged that Midamerica had an interest in The Cleveland Terminals Building Company (in respect of which the proof and the findings are quite to the contrary (F. 29, R. 498)) nevertheless, since (1) The Cleveland Terminals Building Company had no equity in the building occupied by The Higbee Company (F. 32, R. 498-499), (2) the new lease was negotiated solely with The Metropolitan Life Insurance Company, and not with The Cleveland Terminals Building Company (R. 308) and (3) the new lease was a contract between The Higbee Company and The Metropolitan Life Insurance Company and not with The Cleveland Terminals Building Company, it becomes obvious that there never was *even a possibility* that Midamerica could be damaged by anything which Bradley and Murphy, as the owners of the Higbee securities, could do or fail to do.

As pointed out earlier in this brief, none of the assignments of error presents a question of general law concerning which there is any conflict. The Circuit Court of Appeals, in this case, stated the law thus:

> "Wherever one person is placed in such a relation to another that he becomes interested for him or with him in any subject of property or business, he is in such a fiduciary relation that he is prohibited from acquir-

> ing rights in the property or business antagonistic to the person with whose interests he has become associated; * * *." (R. 564-5.)

This is the precise holding in the case of *Irving Trust Co. v. Deutsch*, 73 F. 2d 121, relied on by the petitioner. The facts, however, as found by the three tribunals below, completely repel the existence of any fiduciary relationship or conflict of interest. The Circuit Court of Appeals in its decision points out:

> "The Cleveland Terminals Building Company had only a nominal interest in the building, and the fact that Bradley and Murphy became the owners of the Higbee securities could in no way interfere with any real interest of Midamerica or C.T.B. Hence no fiduciary duty toward Midamerica arose with reference to these securities." (R. 567.)

In the *Irving Trust Company* case the directors had negotiated a contract for their corporation which was "concededly essential to" the business of the corporation. They then took the contract themselves, claiming that they had the right to do so because their corporation did not have the resources to carry it out. The contract proved valuable and the directors realized large profits which the court very properly required them to account for to their corporation.

But again the findings of fact repel any such relationship in the present case. In the first place, Bradley and Murphy conducted the major portion of their negotiations for the purchase of the Higbee securities with Midamerica itself at a time when Midamerica owned them. (F. 1 and 2, R. 492-493.) Moreover, prior to such purchase by Bradley and Murphy, and with the full knowledge of the Young Syndicate, Midamerica voluntarily divested itself of the Higbee securities for the very purpose of enabling them to be sold to Bradley and Murphy. (F. 3 and 6, R. 493.) At no time prior to such purchase by Bradley and Murphy did Midamerica or its new owners, the Young Syndicate,

negotiate for the purchase of these securities nor did they say anything to Bradley and Murphy relative to any desire on the part of Midamerica to acquire them. (F. 16, R. 496.) Finally the lower courts found that the purchase by Bradley and Murphy was not the result of any confidence reposed in them by the Young Syndicate or of any opportunity created by any knowledge or influence obtained through employment by or association with the Young Syndicate (F. 17, R. 496); that at no time, after Midamerica voluntarily disposed of the Higbee securities, did it have any interest in or interest in acquiring them, and at no time did their purchase by Bradley and Murphy hinder or defeat any plans or purposes of Midamerica. (F. 20, R. 496.)

The facts incident to the case of *Meinhart v. Salmon*, 249 N. Y. 458 are nowhere to be found in this case. Petitioner was the owner of the Higbee securities (F. 1, R. 492) and it negotiated with Bradley and Murphy, through its stockholder Ball, for the sale of these very same securities. (F. 2, R. 492.) The petitioner and its stockholders were at all times aware that these securities were to be sold to Bradley and Murphy. (F. 3, R. 493.) In fact, petitioner participated in making the sale possible by distributing these securities to the Ball Foundation for the purpose of sale to Bradley and Murphy. The Young Syndicate, which later became the owner of Midamerica stock, was aware of and consented to this distribution. (F. 6, R. 493.)

We now find the Messrs. Young and Kirby, owners of petitioner's stock, making claim to these securities indirectly through the petitioner, this despite the inability of Young and Kirby to substantiate their direct claims to these securities in the actions which they have now abandoned by acquiescing in the decisions of the Circuit Court of Appeals as stated in petitioner's brief. (Br. 3.)

Hence, as asserted at the beginning of this brief, there is no dispute either between the courts of appeals of the several circuits nor between the parties themselves with

respect to any principle of substantive law. In the last analysis, the holding of the Circuit Court of Appeals in the present case is precisely in accord with the principle of law announced in the *Irving Trust Company* case. The only difference between the two is one of fact. The facts, as found by the courts below, fail totally to support any factual similarity or analogy to the *Irving Trust Company* case. Petitioner seeks here to re-examine and re-argue, as he did in the three tribunals below, the probative value of evidence and inferences to be drawn from testimony, all of which have been thrice determined against him.

Estoppel.

During the trial of these proceedings Midamerica demanded payment by Bradley and Murphy of their note in the amount of upwards of $560,000. (F. 56, R. 503.) Complying with this demand Bradley and Murphy borrowed the necessary sum and paid it in open court to Midamerica. (F. 57, R. 503, R. 470.) Midamerica thereupon addressed a letter to J. P. Morgan & Company admitting Bradley and Murphy's ownership of said securities by authorizing J. P. Morgan & Company to recognize Bradley and Murphy as the owners of a participation in the Higbee securities which was then held by J. P. Morgan & Company for the benefit of itself and others. At the same time Midamerica surrendered to Bradley and Murphy the collateral, which included the Higbee securities. (F. 57, R. 503.) This was at the very time when Midamerica claimed that it was the equitable owner of the very collateral which it surrendered upon payment of the note. It was at the very time when Midamerica sought to seize the Higbee securities by means of a public sale at which, in effect, no one could bid against it. It was at the very time when Midamerica frankly admits that it didn't expect Bradley and Murphy would be able to finance themselves because of the pendency of an appeal by two preferred stockholders attacking the Plan of Reorganization of The Higbee Company, which Plan had been pre-

viously approved by the District Court. (F. 49, R. 502.) It was at the very time when, to protect themselves against Midamerica's scheme to seize the Higbee securities, Bradley and Murphy were compelled to purchase the holdings of these two excepting stockholders. (F. 51, R. 502.) They were obliged to incur the expense necessary successfully to resist the efforts of the principal owner of Midamerica to prevent the dismissal of such appeal. (F. 52, R. 502, F. 54, R. 502.) And finally, after thwarting the efforts of Midamerica to prevent them from financing themselves, Bradley and Murphy borrowed the money and paid it to Midamerica. (F. 57, R. 503.)

Obviously, if Bradley and Murphy were called upon by petitioner to pay the note, such demand and such acceptance of payment by petitioner ratified and validated Bradley and Murphy's purchase from the Ball Foundation. By its demand for payment Midamerica not only placed itself in a position sharply inconsistent with the position which it asserts in these proceedings, but it also expressed its acquiescence in the sale and recognized the right of Bradley and Murphy. Again, as was stated by the Circuit Court of Appeals:

> "Whether this be considered as a binding election of remedies or as an equitable estoppel (*Miller v. Ahrens*, 163 F. 870; *Quinlan v. Myers*, 29 O. S. 500; *Frederickson v. Nye*, 110 O. S. 439), in any case Midamerica is barred from changing its ground after Bradley and Murphy have altered their position substantially for the worse. All of the elements of equitable estoppel are presented. *Railway Co. v. McCarthy*, 96 U. S. 258; *Texas Co. v. Gulf Refining Co.*, 26 Fed. (2d) 394 (C. C. A. 5)."

Laches.

For slightly less than five years the petitioner failed to assert any claim, and waited until after The Higbee Company, through the efforts of Bradley and Murphy, had become a very profitable enterprise. Bradley and Murphy,

with full knowledge of the petitioner, devoted their time and effort over a period of more than four years to place the department store in efficient financial operation. After the hazard was all over, and the skill and knowledge of Bradley and Murphy had made the investment profitable, then, for the first time, petitioner claims the investment. This, equity will not allow. *Harris v. Wallace Mfg. Co.*, 84 O. S. 104; *Alexander v. Phillips Petroleum Co.*, 130 F. 2d 593, 605.

Again petitioner attempts to present to this Court a wholly false issue, that the Circuit Court of Appeals went beyond the matters properly before it and held petitioner to be barred by laches although that question was not raised in the Statement of Points filed by petitioner in the Circuit Court of Appeals, and that the ruling of the Circuit Court of Appeals was contrary to that of the District Court. For the convenience of this Court, the statement in plaintiff's brief (Br. 27) and the Opinion of the District Court are set forth in parallel columns as follows:

Petitioner's Brief Page 27.	**Decision of the District Court R. 525, 526.**
"The Circuit Court agreed with the conclusion of the Special Master (R. 506) and the District Judge (R. 526) that the statute of limitations does not bar this claim, *but overruled the District Court in holding that laches existed irrespective of the statute of limitations.*"	"No justifiable reason has been advanced why Young and Kirby, with knowledge of the Higbee reorganization and the assertion of legal and complete ownership of the Higbee Junior indebtedness and common stock by Bradley and Murphy in that proceedings, took no action for four years to challenge such ownership. If other ground for rejection of such claim were not adequate, this unreasonable lapse of time would support, or alone sustain, a denial of the equitable relief here sought."

Perhaps a word should be said about the assertion by petitioner that it withheld asserting its claim against Bradley and Murphy because it was ordered so to do by the District Court.

There is not one word in the ruling of the Special Master quoted on page 28 of petitioner's brief from which it could be inferred that the Special Master attempted to discourage the filing of claims to ownership of the Higbee securities. He merely stated that he preferred to develop a Plan of Reorganization with dispatch, leaving for future determination the adjudication of the claims which had already been asserted. At that time claims had been asserted by Bradley and Murphy (R. 2, R. 24), by The Cleveland Terminals Building Company (F. 24, R. 497) and by the assignee of The Vaness Company (F. 25, R. 497) but *not* by the petitioner here.

To assert that petitioner relied upon the ruling of the Bankruptcy Court, at a time when other interests had asserted their claims, is to rely upon a ruling which never existed, at a time when the petitioner had no thought of asserting a claim for the very definite reason as stated in the opinion of the Circuit Court of Appeals that the record shows "by convincing evidence that not until after The Higbee Company had become a very profitable enterprise was the present claim asserted." (R. 564.)

CONCLUSION.

In the absence of clear error, this Court will not ordinarily reexamine findings of fact in which both lower courts have concurred. As said by Chief Justice Hughes, on page 558 of the opinion in *Texas & New Orleans R. R. Co., et al. v. Brotherhood of Ry. & Steamship Clerks, et al.,* 281 U. S. 548:

> "On the questions of fact, both courts below decided against the petitioners. Under the well established rule, this court accepts the findings in which two courts concur, unless clear error is shown."

It is not believed that this rule was intended to be abrogated in the recent decision of *Baumgartner v. United States of America,* 88 L. Ed. 1155, wherein Justice Frankfurter said, on page 1158:

> "That the concurrent findings of two lower courts are persuasive proof in support of their judgments is a rule of wisdom in judicial administration. In reaffirming its importance we mean to pay more than lip service."

In *Magnum Import Co., Inc. v. Coty*, 262 U. S. 159, Mr. Chief Justice Taft said, on page 163:

> "The jurisdiction to bring up cases by certiorari from the Circuit Courts of Appeals was given for two purposes, first to secure uniformity of decision between those courts in the nine circuits, and second, to bring up cases involving questions of importance which it is in the public interest to have decided by this court of last resort. The jurisdiction was not conferred upon this court merely to give the defeated party in the Circuit Court of Appeals another hearing."

The questions presented fail to meet either test. There is no conflict of decision. No question of importance to the public is involved. There is presented no question concerning which there is a substantial doubt.

It is therefore submitted that the petition for writ of certiorari should be denied.

Respectfully submitted,

CHARLES K. ARTER,

LEWARD C. WYKOFF,

Attorneys for Charles L. Bradley and John P. Murphy.

(21)

In the Supreme Court of the United States

OCTOBER TERM, A. D. 1944.

No. 496.

In the Matter of
THE HIGBEE COMPANY, *Debtor.*
BANKRUPTCY
No. 36,119.

THE TERMINAL AND SHAKER HEIGHTS REALTY CO.,
Petitioner,

vs.

CHARLES L. BRADLEY and
JOHN P. MURPHY,
Respondents.

PETITIONER'S REPLY BRIEF ON PETITION FOR WRIT.

ROBERT J. BULKLEY,
JAMES A. BUTLER,
Bulkley Bldg., Cleveland 15, Ohio,
ROBERT W. PURCELL,
Terminal Tower, Cleveland 13, Ohio,
Attorneys for The Terminal and Shaker Heights Realty Company.

THE GATES LEGAL PUBLISHING CO., CLEVELAND, OHIO—MAIN 5647

INDEX.

Cases.

In the Supreme Court of the United States

OCTOBER TERM, A. D. 1944.

No. 496.

THE TERMINAL AND SHAKER HEIGHTS REALTY CO.,
Petitioner,

vs.

CHARLES L. BRADLEY and
JOHN P. MURPHY,
Respondents.

PETITIONER'S REPLY BRIEF ON PETITION FOR WRIT.

Three important and very interesting questions of law growing out of the administration of bankruptcy reorganization proceedings involving two large companies are presented in this case.

Respondents' brief deals entirely with the findings of fact as made by the Master and confirmed by the District Court and the Circuit Court of Appeals. We do not now question any facts thus judicially established. Our petition for writ of certiorari is based exclusively on the error of the lower courts in dealing with facts found to exist in this case. This decision of the Sixth Circuit Court is in conflict with the holding of the Second Circuit Court of Appeals in the case of *Irving Trust Co. v. Deutsch*, 73 F. (2d) 121, in that it permits a subsequent judicial determination to justify an exception to the rigid rule of loyalty demanded of corporate officers and directors. The important questions raised in this case, relating to bankruptcy reorganization proceedings and the conduct of corporate officers involved therewith, matters of great general interest, have not been passed upon by the Supreme Court.

On October 9, 1944, the Supreme Court granted a petition for writ of certiorari in pending application No. 342, entitled *"Young v. The Higbee Co., et al."* That case was argued consecutively to the instant case in the Circuit Court of Appeals. It involves facts which respondents have sought to use in this case. The issue in case No. 342 is whether or not J. F. Potts and William Boag, preferred stockholders of the Higbee Company, have the right to keep for themselves the proceeds ($100,000) of the sale to Bradley and Murphy of their appeal against confirmation of the Higbee reorganization plan, then pending in the Sixth Circuit Court. One of the grounds on which Bradley and Murphy in the instant case based their defense of estoppel was their payment of that large sum to Potts and Boag to buy off an appeal, which, if successful, would have benefited all preferred stockholders.

These two cases are intimately bound together. They concern, from different aspects, the same facts growing out of the Higbee Co. bankruptcy reorganization. Wisely, this Court has determined to hear case No. 342 on its merits. A complete determination of the pending questions growing out of the Higbee reorganization, involving all the parties to the transaction which is the subject of the litigation in case No. 342, will require the Court to hear this case on its merits. This case might well be heard either concurrently with or consecutively to case No. 342.

ANALYSIS OF RESPONDENTS' BRIEF.

We offer the following comments on respondents' "Statement of the Case":

(1) The Fiduciary Relationship.

We take issue only with the last two paragraphs on page 3. Respondents assert as a fact found by the Master that "Midamerica had nothing but a nominal interest in CTB (The Cleveland Terminals Building Co.) on May 15,

1937." Reference to the Master's finding 29, as cited, clearly shows that it was not a finding of fact based on any testimony in this case, but a conclusion drawn from a decision of the Sixth Circuit Court of Appeals on April 16, 1941. Thus we are squarely confronted with the question posed in our opening brief, whether as a matter of law a subsequent adjudication of the extent of a corporation's interest may be used to justify conduct of a corporate officer in assuming a position in conflict with the interest of his corporation.

The full text of Master's finding No. 29 (R. 498) follows:

> "29. The decision of the Circuit Court of Appeals on April 16, 1941 (*In re Van Sweringen Company,* 119 F. (2d) 231) holding that the second mortgage was valid as a claim against The Cleveland Terminals Building Company for only $2.00 and that the $13,787,000 claim against the Van Sweringen Corporation was valid as a claim against The Van Sweringen Corporation for only $887, determined that Midamerica never had anything other than a nominal interest in The Cleveland Terminals Building Company."

For the propositions that CTB "had no equity in the building" and that "the real owner of the building together with the lease and rentals was the Metropolitan Life Insurance Company" Master's finding No. 32 is cited. This finding, in fact, shows that CTB *did* have an equity in the Higbee store building subject to a security assignment to the Metropolitan Life Insurance Company. But the Master adds that the "equity has subsequently been determined to be of no value." When and by whom the "subsequent determination" was made, the Master fails to tell. Surely he made no finding that the equity had been determined to be valueless on May 15, 1937. Again we are confronted with the question as to what may be the legal effect of a "subsequent determination" concerning the extent of a corporation's interests, and how far such "subsequent

determination'' may justify the conduct of a corporate officer in assuming a position presently adverse to his corporation.

The full text of Master's finding No. 32 (R. 498) follows:

> ''32. The only interest which The Cleveland Terminals Building Company had in The Higbee Company or in the Higbee store building, during the time involved in this controversy, consisted of an equity in the Higbee store building which was subject to a first mortgage to The Metropolitan Life Insurance Company of upwards of Ten Million Dollars,—the lease with The Higbee Company, together with all past due and unpaid rentals, having been assigned to The Metropolitan Life Insurance Company as a part of the security for the mortgage debt. This equity in the Higbee building has subsequently been determined to be of no value.''

(2) Estoppel.

Assuming as true all the facts as stated by respondents under this heading, we find no allegation which shows a legal detriment to Bradley and Murphy arising from Midamerica's demand that their past due note be paid in accordance with its terms. True, there is a purported ''finding of fact,'' No. 46 (R. 501) by the Master, that Bradley and Murphy changed their position for the worse, but obviously this must be a conclusion of law. What they say they did was to borrow money elsewhere to pay in full their past due note. Surely, they suffered no legal detriment in changing creditors in order to meet a past due obligation.

The full text of Master's finding No. 46 (R. 501) follows:

> ''46. Bradley and Murphy reasonably relied upon said notice in writing and acted thereon so as to change their position for the worse.''

But respondents say that the borrowing of the money was "among other things." The citations that follow (F. 50, F. 51, F. 52, R. 502) show that the "other things" consisted of employing counsel to resist Midamerica's demand for payment of their admittedly past due obligation; of purchasing stock from Potts and Boag, and of causing the dismissal of the appeal which Potts and Boag had taken to the Sixth Circuit Court. The purchase of stock and dismissal of the appeal are the subject matter of Case No. 342 in this Court and are discussed herein below.

(3) Laches.

Respondents' brief quotes from the decision of the District Judge (R. 525-6) wherein he commented upon the delay of four years in the commencement of this action. Although the District Judge may have felt that the time elapsed between the purchase of the Higbee securities by Bradley and Murphy and the commencement of this action by Midamerica was too long, nevertheless, he affirmed the conclusion of the Master that laches did not bar recovery herein.

The Master's Ad Interim report contains conclusion of law No. 14 (R. 506) specifically holding that Midamerica's claim was not barred by laches. The full text of Master's conclusion No. 14 (R. 506) follows:

> "14. Section 77B (b) and Section 261 of Chapter X of the Bankruptcy Act as to reorganizations of corporations provide that all periods of time prescribed by statutes of limitation shall be suspended during the pendency of a reorganization proceeding. This is applicable to this proceeding, so that the bar of a statute of limitations by laches or otherwise is not enforceable in this proceeding."

The opinion of the District Judge expressly approves all findings of fact and conclusions of law made by the Master in the following language (R. 526):

"I think that the findings and conclusions of the Master are adequately supported and respond to the evidence, and they are approved and adopted and the report confirmed."

These findings and conclusions were reaffirmed by the District Court's ruling as expressed in its Journal Entry finally disposing of this case on March 16, 1943 reading in part as follows (R. 530):

"It is therefore ORDERED, ADJUDGED AND DECREED that:

1. The ad interim report of the Special Master heretofore filed herein, is hereby, in all respects, ratified, approved and confirmed, and the objections and exceptions filed thereto are overruled."

Therefore, the argument on page 27 of Petitioner's main brief is a correct and accurate statement. The Circuit Court did overrule the District Court on the question of laches, although respondents took no exception to the order of the District Court cited above.

Midamerica, through its counsel, was closely following the progress of the Higbee reorganization and relied upon the rulings of the Special Master concerning claims to these Higbee securities, all as more fully set forth on pages 28 and 29 of petitioner's first brief. Obviously Midamerica was not "ordered" to withhold asserting its claim. Respondents' characterization of our position at the bottom of page 12 of their brief, and the ensuing discussion distort petitioner's contentions.

Conflict of Interest.

In its opinion the Circuit Court did not sustain respondents' contention that there was no conflict of interest. On the contrary, the court's opinion (R. 566) says:

"If CTB had any substantial interest in this matter, and if its claim were not barred by estoppel and laches,

we think that a substantial conflict of interest would have been created between the parties."

In so far as respondents now advance the argument that a conflict of interest did not exist, it is they who are asking for a review of the findings of the court. Our argument assumes that a conflict of interest existed, but for the three legal points specifically mentioned in the court's opinion, which are the three points we have just discussed, and now seek to have reviewed by this Court.

From the language in the opinion it appears that the Circuit Court's conclusion that there was a lack of substantial interest, was based upon a subsequent adjudication. The question of conflict of interest should be determined on the basis of the situation as it existed at the very time that Bradley and Murphy bought the Higbee securities, namely May 15, 1937. True, at that time CTB was in arrears as to mortgage interest and had assigned the Higbee lease to the Metropolitan Insurance Company as additional security for the mortgage on the building. However, as soon as Bradley and Murphy, by their purchase of the Higbee securities identified themselves with the Higbee interests for lower rents, as against the CTB interests for higher rents, the Special Master in charge of the CTB bankruptcy reorganization proceedings moved to have CTB's interest protected by the appointment of independent counsel. The District Court thereupon appointed Walter Sharp as independent counsel for CTB. This action of the court clearly shows that in the situation as it existed at the time, there *was* a conflict of interest.

The officers thus placed themselves in a position which was judicially determined *at the time* to be in conflict with the interests of their corporation. To hold that such conduct could be justified by the *subsequent* defeat of Midamerica's claims, direct and indirect, against CTB and Higbee, is to give them a personal interest in defeating

the claims which their own corporation was asserting. Such a rule accomplishes the utmost possible of disintegrating erosion against the principle of undivided loyalty of corporate officers to their employers. It is unprecedented, unsound and immoral to hold that the subsequent defeat of a corporation in litigation pressed in good faith, can be a justification to corporate officers for taking a position which they must have known at the time to be adverse to their corporation.

The Sixth Circuit Court in the instant case declined to hold Bradley and Murphy accountable to petitioner on the ground that Midamerica's interest in the situation was "not substantial," because of two decisions by the same Sixth Circuit Court; one in the case of *Higbee Co. v. Cleveland Terminals Building Co.*, 106 F. (2d), 796, decided two years after the cause of action in the instant case arose, and the other in the case of *In re Van Sweringen Company*, 119 F. (2d) 231, decided four years after this cause of action arose.

Further reference seems justified to the extraordinary contention made at the bottom of page 6 of respondents' brief. This refers to the adjudication by the Sixth Circuit Court in 1941, in *Re Van Sweringen Company*, 119 F. (2d) 231, reducing certain claims owned by Midamerica to nominal amounts and holding that, "*in the hands of Midamerica* they never represented more than a nominal interest." (Italics ours.)

The Circuit Court there gave as reason for the disability of Midamerica in this respect, that in its inception Midamerica was made the instrumentality of certain financial interests to regain for their own use, and at the expense of their creditors, a lost railroad holding company empire, by the purchase of securities at a sale forced by J. P. Morgan & Co. The Van Sweringen brothers and their associates, having secured new financial backing, were found to have deserted the corporations to which they owed a loyalty and to have acquired the securities at bargain prices for

their own personal interests through the instrumentality of Midamerica, which they had caused to be incorporated for that purpose. It was this transaction that the Circuit Court held created a disability to Midamerica in asserting its claims. Among those named in that decision of the Circuit Court as having been associated with the Van Sweringens in the disloyalty which disabled Midamerica, were *Charles L. Bradley* and *John P. Murphy.* The same Bradley and Murphy now rely upon that decision to relieve them from the consequences of assuming a conflicting position in 1937.

SUPREME COURT CASE 342.

In November, 1941, J. F. Potts and William W. Boag, who owned preferred stock of Higbee and who purported to represent preferred stockholders generally in the reorganization proceedings, appealed from the order of the District Court which had approved the Higbee plan of reorganization. There were several grounds for the appeal, among which were the following:

First, it was urged that the junior indebtedness of Higbee, upon which Bradley and Murphy had filed their claims, should be considered a capital contribution to Higbee, because it represented an advance by CTB made in 1931—when Bradley was President of CTB—while Higbee was controlled by CTB.

Second, it was urged that in the alternative, pursuant to the rule of *In re Van Sweringen Company, supra,* the junior indebtedness should be allowed only in the amount of $100,000 because that was the amount which Midamerica had paid for the junior indebtedness when J. P. Morgan & Co. foreclosed and sold it at auction on September 30, 1935 —Bradley being at the time a director of both Midamerica and of Higbee.

Third, as a second alternative it was urged that, pursuant to the same rule, the junior indebtedness upon which Bradley and Murphy had asserted their claim should be allowed against Higbee for no more than $600,000, that being the purchase price which Bradley and Murphy had agreed to pay for it—Bradley being at the time a director of Higbee.

(The foregoing appears at pages 182 and 183 of the transcript of the record in case No. 342, now pending in the October, 1944, term of this Court. Bradley and Murphy were parties in that case below.)

Apparently Bradley and Murphy felt that their interests required that these contentions be disposed of without final judicial determination. Therefore on March 7, 1942, Bradley and Murphy paid Potts and Boag $115,000 for the 260 shares of Higbee preferred stock then owned by Potts and Boag, which had a market value of approximately $15,000. Bradley and Murphy thus came to control the appeal which Potts and Boag had theretofore perfected and they promptly caused its dismissal, in complete disregard of the interests which other preferred stockholders had in that appeal. Potts described the transaction as "selling the appeal." (R. 188 in case No. 342.)

On October 9, 1944, this Court granted a petition for writ of certiorari in case No. 342 (Robert R. Young v. The Higbee Co., *et al.*) and will hear and determine the question of the propriety of the conduct of the parties to that transaction. Bradley and Murphy were directors of Higbee, a debtor in reorganization proceedings,—and thus in a very real sense officers of the court—at the time they made this payment to Potts and Boag. In No. 342, this Court will consider the conduct of Potts and Boag, appellants in behalf of preferred stockholders in "selling the appeal" for their own benefit. In the instant case this Court should consider the conduct of Bradley and Murphy, officers of The Higbee Co. and of the Bankruptcy Court, in buying the same appeal for their own purposes.

The legal detriment which Bradley and Murphy claim and which at page 11 of respondents' brief they state caused an estoppel, resulted from the payment of the $100,000 bonus to Potts and Boag to bring about a dismissal of the appeal. A similar contention was strenuously urged below. The Circuit Court regarded this purchase of the Potts and Boag stock and the consequent dismissal of the appeal as a legitimate, proper transaction. However, if upon a hearing of case No. 342 this Court should reverse the Circuit Court and hold that the purchase from Potts and Boag under the circumstances, and the subsequent dismissal of the appeal, constituted an unlawful transaction in which Bradley and Murphy participated, then the ground for equitable estoppel asserted by Bradley and Murphy would be eliminated.

This is a case in equity to impress a constructive trust. The Circuit Court balanced the equities and refused to impress the trust. One of the important equities relied upon by respondents was the detriment incurred because they paid a bonus to Potts and Boag in a transaction which the Circuit Court approved. Should this Court reverse the Circuit Court in case No. 342, then that equity which the Circuit Court found to be in favor of Bradley and Murphy would no longer exist. In order to do justice to the parties here, this Court should also review the decision of the Circuit Court in the instant case.

CONCLUSION.

Respondents' conclusion makes a final attempt to persuade this Court that petitioner is seeking a re-examination of the facts involved in this litigation. That is not our purpose. Petitioner contends that under the facts as they have been judicially determined in this case, the Circuit Court has improperly applied the law with the result that this judgment of the Sixth Circuit Court is in conflict with the Second Circuit Court of Appeals in the case of *Irving Trust*

Co. v. Deutsch, 73 F. (2d) 121. The Second Circuit Court holds fiduciaries strictly accountable to their cestuis and allows no exceptions to that rule.

The questions presented in this petition for writ of certiorari are important and it is in the public interest to have them decided by the Supreme Court. Dealing as they do with bankruptcy reorganization proceedings, they concern business generally. The overreaching conduct of corporate officers serving during the course of bankruptcy reorganization, under the administration of the courts, is a matter of great concern which should now be passed upon by the Supreme Court. Petitioner requests this Court to grant a writ of certiorari to the Sixth Circuit Court of Appeals in this case.

Respectfully submitted,

ROBERT J. BULKLEY,
JAMES A. BUTLER,
ROBERT W. PURCELL,
Attorneys for the Petitioner.